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Report to the Chairman, Committee on Energy and Commerce, House of Representatives

March 1992

LONG-TERM CARE INSURANCE

Better Controls Needed in Sales to People With Limited Financial Resources

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Human Resources Division

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The Honorable John D. Dingell
Chairman, Committee on Energy and Commerce
House of Representatives

Dear Mr. Chairman:

This report responds to your March 12, 1991, letter that expressed concern about low-income older people who may be sold long-term care insurance policies that are not appropriate for their financial status. Although long-term care insurance is expensive, people with relatively limited financial resources have purchased such policies. In many instances, the benefits may not meet their needs.

Long-term care insurance is growing in popularity as the cost of long-term care climbs and many older people find that they have little protection from these costs. Nursing home care, which accounts for the vast majority of long-term care expenses, costs about $25,000 a year. In some cases, the annual cost of this care approaches $75,000. In 1990, about 45 percent of nursing home costs were paid by nursing home residents and their families. Another 45 percent was paid by Medicaid, the primary government program financing long-term care services for certain categories of low-income people. A combination of other government and private sources paid the remaining costs.

In discussions with your office, we agreed to provide information on (1) health and financial factors that limit the purchase of long-term care insurance and (2) company policies regarding the sale of long-term care insurance to low-income people and the extent to which companies train and monitor agents to comply with such policies.

The results of our work are summarized below and discussed more fully in appendixes I and II.

Results in Brief

Both health and financial factors limit the number of older people able to purchase long-term care insurance. For example, 23 percent of people age

65 may not be able to obtain coverage because of health problems.[1] Between 79 and 90 percent of people age 67 or older could not afford long-term care insurance in 1990.[2] People with limited financial resources generally should not purchase long-term care insurance because they (1) cannot afford adequate coverage, (2) may quickly "spend down"[3] to Medicaid's eligibility level, or (3) may already be covered by Medicaid. Nevertheless, a 1990 survey found that almost 30 percent of people buying such insurance had annual incomes below $20,000.[4]

Our work at eight insurance companies found that, except for Medicaid recipients, companies are doing little to prevent the sale of long-term care insurance to low-income people. Officials from these companies told us that their policy is to avoid selling this insurance to low-income people. However, this policy is not always articulated in writing, and companies' actual practices are difficult to determine.

Despite their stated intentions, the companies have few controls over such sales. Only one of the eight companies has established financial criteria for who should be buying long-term care insurance (people with nonhousing assets of $20,000 or more), and none obtains information that would help determine a person's income or assets. Most of the training material that companies use for their agents is vague or silent about how or whether an agent should consider a consumer's income and assets when selling long-term care insurance. In addition, companies do not specifically monitor whether agents sell this insurance to low-income people. Agent

[1]Christopher Murtaugh and Peter Kemper, "Risky Business: Long-Term Care Insurance Underwriting," Agency for Health Care Policy and Research, Department of Health and Human Services. Paper presented at the annual meeting of the Association for Health Services Research, San Diego, California, June 30-July 2, 1991.

[2]Alice M. Rivlin and Joshua M. Wiener, Caring for the Disabled Elderly: Who Will Pay?, the Brookings Institution (1988). This study concluded that older people cannot afford such insurance based on assumptions about their age, health status, income and assets, and other factors.

[3]The term generally refers to the process by which people deplete their income and assets to Medicaid eligibility levels. For example, a person may have a monthly income of $400 but the state's income standard is $350. A person must incur $50 in medical expenses before becoming eligible for Medicaid.

[4]Marc Cohen, LifePlans, Inc. Paper presented at the Seventh Annual Conference on Private Long-Term Care Insurance, Baltimore, Maryland, June 26-28, 1991.

commissions can be substantial, providing an incentive to sell policies to people who do not need them.[5] Moreover, marketing materials from half of the companies do not caution consumers to consider whether long-term care insurance is appropriate, given their particular income and assets.

Background

Long-term care refers to an array of medical, social, and support services delivered over an extended period of time to people in nursing homes or in the community who are dependent on others for assistance. Private long-term care insurance, a relatively new but growing product, pays only a small portion of total long-term care expenditures. The Health Insurance Association of America (HIAA) estimated that, in 1990, about 1 percent of long-term care expenditures was paid by long-term care insurance.

Although few insurance companies sold long-term care insurance before 1986, the number of companies and policies has recently increased. HIAA reported that 143 companies sold about 1.9 million long-term care insurance policies from about 1985 through 1990. Some people purchase these policies to protect their assets against possible future long-term care expenses. Other people buy this insurance because they are uncertain about the quality and availability of long-term care provided through Medicaid.

Policies vary considerably in cost, services covered, amounts payable for a day of service, duration of coverage, and other conditions. In addition, policies that offer similar benefits can differ substantially in price. For example, we recently found that yearly premiums for six similar individual policies that covered nursing home care and home health care ranged from about $1,200 to $3,000 if purchased at age 75.[6]

Generally, insurance is sold on a personal, one-to-one basis. Most companies sell through "captive" agents (employees who sell only one company's product), "independent" agents (agents or brokers who sell products offered by multiple companies), or both. Some companies sell policies through direct mail without an agent or through financial planners.

[5] Long-Term Care Insurance: Risks to Consumers Should Be Reduced (GAO/HRD-92-14, Dec. 26, 1991).

[6] Long-Term Care Insurance: Consumers Lack Protection in a Developing Market (GAO/T-HRD-92-5, Oct. 24, 1991).

To help states monitor variations in policies and sales practices, the National Association of Insurance Commissioners (NAIC), a nonprofit organization of state insurance commissioners, has developed a model act and model regulations. As the market has matured, NAIC has amended its models. The model act and regulations attempt to balance the need for consumer protection with the need for innovation and flexibility in the development of this market. To varying degrees, states have adopted sections of these model regulations. Insurance companies must comply with these regulations in states where they have been adopted.

Scope and Methodology

To provide information on financial factors that limit the purchase of long-term care insurance, we reviewed two studies: one by researchers at the Brookings Institution, and the other by the Families USA Foundation and the United Seniors Health Cooperative. We also reviewed research conducted by the Agency for Health Care Policy and Research of the Department of Health and Human Services, which addresses the elderly population that may not be able to obtain long-term care insurance because of health problems.

To provide information on companies' sales policies, we obtained information from eight companies that sell individual long-term care insurance policies nationally. We selected these companies because information obtained from insurance companies and other sources indicated that, as of December 1990, their long-term care business collectively represented about one-half of the policies sold in this country. One of the eight companies sold policies through captive agents only, two sold through independent agents only, and four sold through both. One company sold through direct mail without the aid of agents.

Because we had limited access to the insurance companies' records and did not observe company practices and agent behavior first-hand, we relied on information the companies provided us. We obtained and reviewed each company's long-term care insurance policies, outlines of coverage, policy applications, agent training manuals, underwriting guidance for agents, and marketing material. When necessary, we interviewed officials from the companies to obtain clarification of these materials. We also interviewed officials to determine the companies' policies regarding sales to low-income people.

We obtained national data on the long-term care insurance industry from HIAA. We obtained information on relevant model state regulations from NAIC.

We conducted our review between June and October 1991 in accordance with generally accepted government auditing standards.

As agreed with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 15 days after its issue date. At that time, copies of this report will be sent to interested congressional committees and other parties on request. If you or your staff have any questions about this report, please call me at (202) 512-7118. Other major contributors are listed in appendix III.

Sincerely yours,

Mark V. Nadel

Mark V. Nadel
Associate Director, National and
Public Health Issues

Contents

Abbreviations

HIAA	Health Insurance Association of America
NAIC	National Association of Insurance Commissioners

Financial and Health Factors Influence Who Can Buy Insurance

Long-term care insurance is expensive. People with limited financial resources should not buy it because many of them are eligible for government assistance. Other people could become eligible for assistance soon after incurring costs for nursing home care. Because of its high cost, most older people are not able to buy long-term care insurance. Moreover, many people, regardless of their age or financial status, are precluded from buying this insurance because insurance companies consider them to be an unacceptable health risk.

Long-Term Care Insurance Is Not Appropriate for People With Limited Financial Resources

Long-term care insurance can be expensive and is generally not appropriate for people with limited financial resources. People who are covered by Medicaid, a medical assistance program funded by federal and state governments, generally do not need long-term care insurance because Medicaid will pay for their care. Long-term care insurance may also be inappropriate for people who have incomes and assets so low that the expenses of a nursing home stay would soon make them eligible for Medicaid. To be eligible for Medicaid benefits, people must substantially deplete their income and assets.

Problems that face many purchasers of long-term care insurance may be intensified for policyholders with limited financial resources. A survey sponsored by the Health Insurance Association of America found that 29 percent of people buying such insurance had annual incomes below $20,000.[1] Purchasers with limited financial resources are particularly vulnerable to premium increases that could make it difficult for them to retain their policies. As a result, they could lose the investment value of their policy because many policies do not contain "nonforfeiture benefits." That is, policyholders who allow their policies to lapse will not get back a portion of the money they have paid in premiums.[2]

A recent study showed that people with less than $10,000 in nonhousing assets probably should not buy even the most basic policy. The study also

[1] Cohen, LifePlans, Inc.

[2] As with whole-life policies, most long-term care insurance policies have fixed annual premiums. Insurers price such policies so that they accrue substantial investment reserves in the early years to cover the increased risks for insurers in the later years. However, unlike whole-life policies, long-term care policies generally do not return any of the investment reserves to policyholders who allow their policies to lapse.

showed that certain long-term care policies probably are not appropriate for people with assets of $25,000 or less.[3] These conclusions are based on the assumption that people without substantial assets have little motivation to purchase this coverage because the cost is too high to protect assets at such levels.

Most Older People Cannot Afford Insurance

Two studies that examined the ability of older people to purchase long-term care insurance found that most older people cannot afford it. The studies' estimates of the population that cannot afford this insurance differ because the researchers used different assumptions about the age of purchasers, income and asset criteria, and prices and coverage of policies.

A study by the Brookings Institution showed that, from 1986 to 1990, 79 to 90 percent of people age 67 or older were not able to afford long-term care insurance.[4] To obtain these estimates, the researchers assumed that people age 67 or older with $10,000 or more in nonhousing assets could spend up to 5 percent of their income on this insurance. The low estimate of 79 percent assumed that a less expensive, low-option policy was purchased; the high estimate of 90 percent assumed a more expensive policy with a higher daily benefit was purchased.

A second study conducted by the Families USA Foundation and the United Seniors Health Cooperative in 1990 showed that 84 percent of people between age 65 and 79 could not afford to pay the average cost of basic long-term care insurance policies from nine leading companies.[5] (See table I.1.) The estimates were obtained by assuming that people would be unable to afford a policy if the sum of their medical expenses and insurance premiums was greater than 10 percent of their income and nonhousing assets.[6]

[3]Stephen C. Goss, Who Should Buy Long-Term Care Insurance? What Type of Policy Makes Sense? Presented at the Sixth Annual Conference on Private Long-Term Care Insurance, March 1990.

[4]Rivlin and Wiener, Caring for the Disabled Elderly: Who Will Pay?

[5]James P. Firman and Susan Polniaszek, The Unaffordability of Nursing Home Insurance, Families USA Foundation and the United Seniors Health Cooperative (Jan. 1990).

[6]Excluded from these assets is the first $12,000 or 50 percent of assets, whichever is greater. Medicaid standards allow individuals to exclude these assets in qualifying for benefits.

Table I.1: People Age 65 to 79 Who Cannot Afford Long-Term Care Insurance Premiums for an Average Cost Policy, by Age (1990)

Age of individual	Percent who cannot afford long-term care insurance
All (65-79)	84
65-69	79
70-74	85
75-79	90

Source: Firman and Polniaszek, The Unaffordability of Nursing Home Insurance, Families USA Foundation and the United Seniors Health Cooperative (Jan. 1990).

Companies Will Not Insure People With Health Problems

In addition to financial limitations, health problems can preclude older people from obtaining insurance. Through a practice known as underwriting, insurance companies identify and classify the potential risk a person or group of people represent. As a result, some people are precluded from purchasing insurance because health problems are believed to make them too great a financial risk. Recent research conducted by the Agency for Health Care Policy and Research, Department of Health and Human Services, showed that in 1990, as many as 23 percent of people age 65 could be rejected for long-term care insurance because of health problems. If the group of people age 65 in 1990 wait until they are age 75 in the year 2000 to apply for insurance, 30 percent could be rejected.[7]

Underwriting practices vary widely among companies. Because not all companies apply the same standards, the researchers separated people who could be rejected into two groups: people "probably" rejected and those "possibly" rejected. They estimated that 12 percent of people age 65 would probably not be able to obtain long-term care insurance because of health problems (20 percent at age 75). People would probably be rejected if they were or had been nursing home residents; had functional limitations; or had major medical problems, such as emphysema, cirrhosis of the liver, or cancer.

[7]Murtaugh and Kemper, 1991.

Eleven percent of people age 65 (10 percent at age 75) would possibly not be able to obtain insurance. These people might be rejected, but would be more likely to obtain insurance than those probably rejected. People would possibly be rejected if they had vascular problems or risk factors, such as heavy drinking or obesity. The results of this research are summarized in table I.2.

Table I.2: Percent of Older Population That Could Be Rejected for Long-Term Care Insurance Because of Health Reasons (1991)

Likelihood of rejection	Age 65	Age 75
Probably rejected	12	20
Possibly rejected[a]	11	10
Either	23	30

[a]Excludes people counted as probably rejected.

Source: Murtaugh and Kemper, "Risky Business: Long-Term Care Insurance Underwriting," Agency for Health Care Policy and Research, Department of Health and Human Services, 1991.

This research simulated a one-stage underwriting approach in estimating the portion of people who might be rejected for insurance. The approach assumed that applicants would be accepted or rejected based solely on their application responses. The researchers were not able to determine the extent to which insurance companies use this "simple" approach in underwriting and acknowledge that some companies employ more sophisticated approaches.

Companies' Efforts to Control Sales to Low-Income People Are Limited

Officials from the eight insurance companies we reviewed said that they do not want to sell long-term care insurance to people for whom it is inappropriate, including low-income people. However, company policies are not always stated in writing. Officials from most companies told us that their companies will not under any circumstances sell insurance to people who are covered by Medicaid. However, an official at one company said that individuals eligible for Medicaid are advised not to apply for a policy, although the company does not refuse them coverage.

Officials at three companies said that it is simply good business to avoid selling to low-income people. Two of these companies' officials explained that an insurance company may incur substantial administrative costs when it makes a sale, only to find that the policyholder cannot afford to continue paying premiums.

Despite their stated intentions, the companies we reviewed do little to avoid selling long-term care insurance to low-income people. The companies generally do not (1) have clearly established financial criteria for determining or advising who should not buy insurance, (2) obtain information regarding the income or assets of applicants, (3) provide training material instructing agents to consider the financial condition of potential buyers and to avoid sales to low-income people, (4) monitor whether agents sell to such people, or (5) distribute marketing material informing low-income people that long-term care insurance might not be appropriate for them. Table II.1 shows the controls that are in place at each of the eight companies.

Table II.1: Eight Companies' Controls Over the Sale of Long-Term Care Insurance to Low-Income People (1991)

	Insurance companies							
	A	B	C	D	E	F	G	H
Application asks about Medicaid eligibility	Yes	Yes	Yes	Yes	Yes	No	No	Yes
Company establishes income/asset criteria	No	No	No	No	No	No	Yes	No
Application asks income/asset data	No	No[a]	No	No	No	No	No	No[a]
Training material for agents covers avoiding sales to low-income people	No[b]	Yes	Yes	Yes	No	No	[c]	No
Company specifically monitors agents' sales to low-income people	No	No	No	No	No	No	[c]	No
Marketing material cautions consumers to consider income and assets	Yes	Yes	No	Yes	No	No	Yes	No

[a]Company officials said that agents are instructed to ask applicants for income and asset information, but they do not record this information on the application.

[b]Company does not have an agent training manual for long-term care insurance.

[c]Company sells long-term care insurance only through direct mail and does not use agents.

Companies provide an agent with a commission for each sale. Agent commissions can be substantial, providing an incentive to sell policies to people who do not need them. For example, we recently found that, on average, commissions account for 60 percent of the total value of a first year premium.[1] Such commissions could encourage agents to inappropriately sell long-term care insurance policies to low-income people.

Companies Lack Criteria and Data to Assess Who Should Buy Insurance

The companies we reviewed do not control the sale of long-term care insurance to low-income people, in part, because they lack criteria about who should buy it and do not obtain financial information from applicants. Seven of the companies have not established financial criteria for who should or should not buy this insurance. Furthermore, companies do not know if they are selling to low-income people because they do not systematically obtain financial information from applicants.

[1]Long-Term Care Insurance: Risks to Consumers Should Be Reduced (GAO/HRD-92-14, Dec. 26, 1991).

Only one company establishes a minimum income or asset level that would indicate long-term care insurance may not be an appropriate purchase for an individual. This company recommends that, because long-term care insurance can help protect assets, it should be purchased by people with nonhousing assets of $20,000 or more. Still, the company believes that the decision to purchase insurance should be left to the consumer. An official from another company told us that he believes this product is inappropriate for people with assets below $50,000 or over $2 million, but his company does not take an official position on such criteria.

None of the eight companies' applications ask for income or asset information that would enable them to determine whether long-term care insurance is suitable for an individual. Officials from two companies said that their agents ask for income and asset information to help determine if insurance is appropriate for a consumer, but this information is not recorded on the application. Officials from four other companies indicated that they believe it is inappropriate or intrusive to ask for income and asset information, and two of these companies' officials added that older people are particularly sensitive to such queries.

The National Association of Insurance Commissioners recognizes that long-term care insurance may not be an appropriate purchase for Medicaid recipients. Its model regulations include a requirement that long-term care insurance applications ask consumers if they are covered by Medicaid. Officials from seven of the companies in our review said that their companies will not sell long-term care insurance to people who are covered by Medicaid. An offical from the remaining company said that her company advises against sales to low-income people. However, two companies do not include a question about Medicaid coverage in their applications.

Training Material Says Little About Avoiding Sales to Low-Income People

Since we did not attend the companies' training courses, we could not fully determine the extent to which companies train their agents to consider an individual's financial status when selling long-term care insurance. However, we did review the companies' training materials and inquire about their training requirements. Officials from most of the companies told us that their agents are instructed not to sell to low-income people. Yet, the companies provide agents with limited training or material on how to (1) assess the financial condition of potential buyers or (2) avoid sales to low-income people.

Three of the companies we reviewed have training material that includes guidance on considering a consumer's financial situation when selling long-term care insurance. As part of their training, these companies provide agents with a code of conduct that encourages agents to only sell insurance to people who can afford it. However, none of the companies' training material provides specific guidance on how to determine if a consumer can afford coverage. Most companies we reviewed sell long-term care insurance through agents; one sells exclusively through the mail. Table II.2 shows the types of agents and the training requirements of the companies we reviewed.

Table II.2: Eight Companies' Use of Agents and Their Requirements for Training (1991)

Number of companies	Type of agents	Training requirement
Four	Captive and independent	Two companies require training for all agents Two companies require training only for captive agents
Two	Independent only	No training required
One	Captive only	[a]
One	No agents	[b]

[a]We could not determine the company's training requirements because training decisions are left to individual branch offices.

[b]Not applicable.

Not all companies require their agents to attend training courses. Officials of two companies, which do not require training for their independent agents, said that they mail bulletins to their independent agents. We were unable to determine whether the bulletins included guidance on selling long-term care insurance because the companies could not readily provide us with copies.

Officials from two of the companies that require training told us that their courses stress that buying long-term care insurance is a way to protect one's assets and, thus, it should be sold to people who have assets to protect. An official from one of these companies, and an official from a third company, said that agents who are required to attend training are instructed to ask applicants about their incomes and assets and to consider this information when making a sale.

Companies Do Not Specifically Monitor Sales to Low-Income People

The seven companies that sell through agents do not specifically monitor whether agents sell long-term care insurance to low-income people. Three companies systematically monitor the distribution of required consumer information on long-term care insurance. Company officials say that agents are disciplined if they do not meet company standards, but none could tell us if, or how frequently, they disciplined agents for selling to low-income people or not providing required consumer information.

Officials of these seven companies said that they monitor their agents' performance to determine whether agents are meeting professional and productivity standards. One way that the companies assess agents' performance is by monitoring the rate at which policies are renewed. This practice is not intended to detect sales to low-income consumers, yet some company officials explained it may have this effect. A low renewal rate means an agent is not sustaining business, and this could mean the agent is selling to people who cannot afford to continue paying premiums. However, since companies do not collect financial information from their policyholders, they do not know the income of people who allow their policies to lapse.

Officials at two companies said that their firms have a second method of monitoring agents—verifying the accuracy of application information through follow-up telephone calls. Although not the primary purpose of these calls, the officials said that on rare occasions their companies learn that an applicant is covered by Medicaid, even though an agent may have indicated otherwise on an application.

Few companies monitor their agents' distribution of a long-term care insurance shopper's guide. NAIC has developed such a guide, and some states have developed their own using NAIC's guide as a model. The guides provide information on Medicaid's coverage of long-term care expenses and they discourage insurance purchases by people whose only source of income is a minimum Social Security benefit or Supplemental Security Income. One section of NAIC's model regulations requires that companies give a shopper's guide to consumers. This provision had been adopted by 12 states as of October 1991. Officials from three companies said that they distribute these guides in all states; officials from five companies said that they distribute them only in the states that require it. However, not all companies monitor the distribution of shopper's guides. Three companies monitor their distribution by asking applicants to sign an acknowledgment that they have received a guide. Officials from another company said that

they monitor distribution of guides through follow-up telephone calls to applicants.

Officials at the seven companies with agents said that agents will be disciplined if it is discovered that they do not meet company standards. However, officials from six of these companies said that they did not have records to indicate whether agents had been reprimanded or terminated specifically for selling to low-income people or for not distributing a shopper's guide. The remaining company did not provide us with information on this subject. Officials from several companies said that they believe that because low-income people cannot afford long-term care insurance, they generally do not buy it. Therefore, there is little need to discipline agents for making such sales. Furthermore, one official said that since the company terminates agents if a certain portion of the policies they have sold are not renewed, agents naturally concentrate on selling to people who can afford to purchase and renew their policies.

Companies Provide Limited or No Guidance to Consumers

Although all eight companies told us that they try to avoid selling long-term care insurance to people with low incomes, only four companies provide consumers with marketing material that alerts them to potential problems of affordability. The brochures and informational letters of the other four companies do not address this issue.

Four companies' marketing material suggests that long-term care insurance may be an inappropriate purchase for people with limited incomes. One company's marketing brochure recommends this product only to people with nonhousing assets of $20,000 or more, and it also advises individuals who might qualify for Medicaid that they do not need this coverage and should not apply for it. Two other companies inform consumers that it is important to buy only what they can afford. The fourth company advises consumers that long-term care insurance may not be appropriate for everyone, especially people who qualify for Medicaid.

Major Contributors to This Report

Human Resources Division, Washington, D.C.

Janet L. Shikles, Director, Health Financing and Policy Issues
(202) 512-7119
Albert B. Jojokian, Assistant Director
Maryanne P. Keenan, Assignment Manager

Los Angeles Regional Office

Ronald G. Viereck, Regional Management Representative
Lori A. Weiss, Evaluator-in-Charge
Leslie A. Miller, Evaluator
Krista M. Perreira, Evaluator